

The Outlook for Education Investing



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The Parthenon Group
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The Outlook for Education Investing Agenda



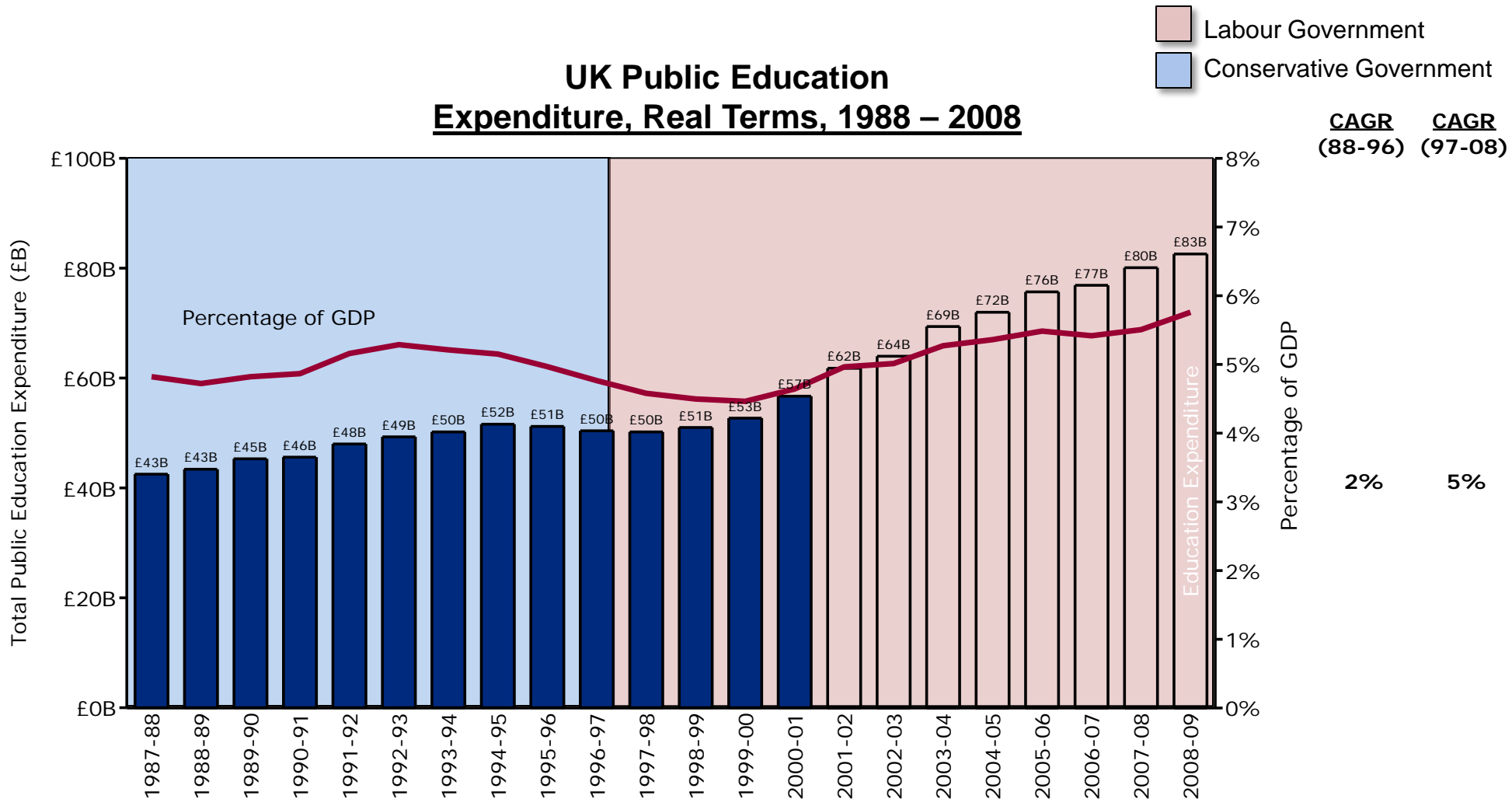
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- Historic evolution of education spending
- Current situation and outlook
- Role of the private sector
- Opportunities for private equity

Funding for education has grown at 2% per annum since 1988, increasing to 5% per annum under the Labour government over the last decade



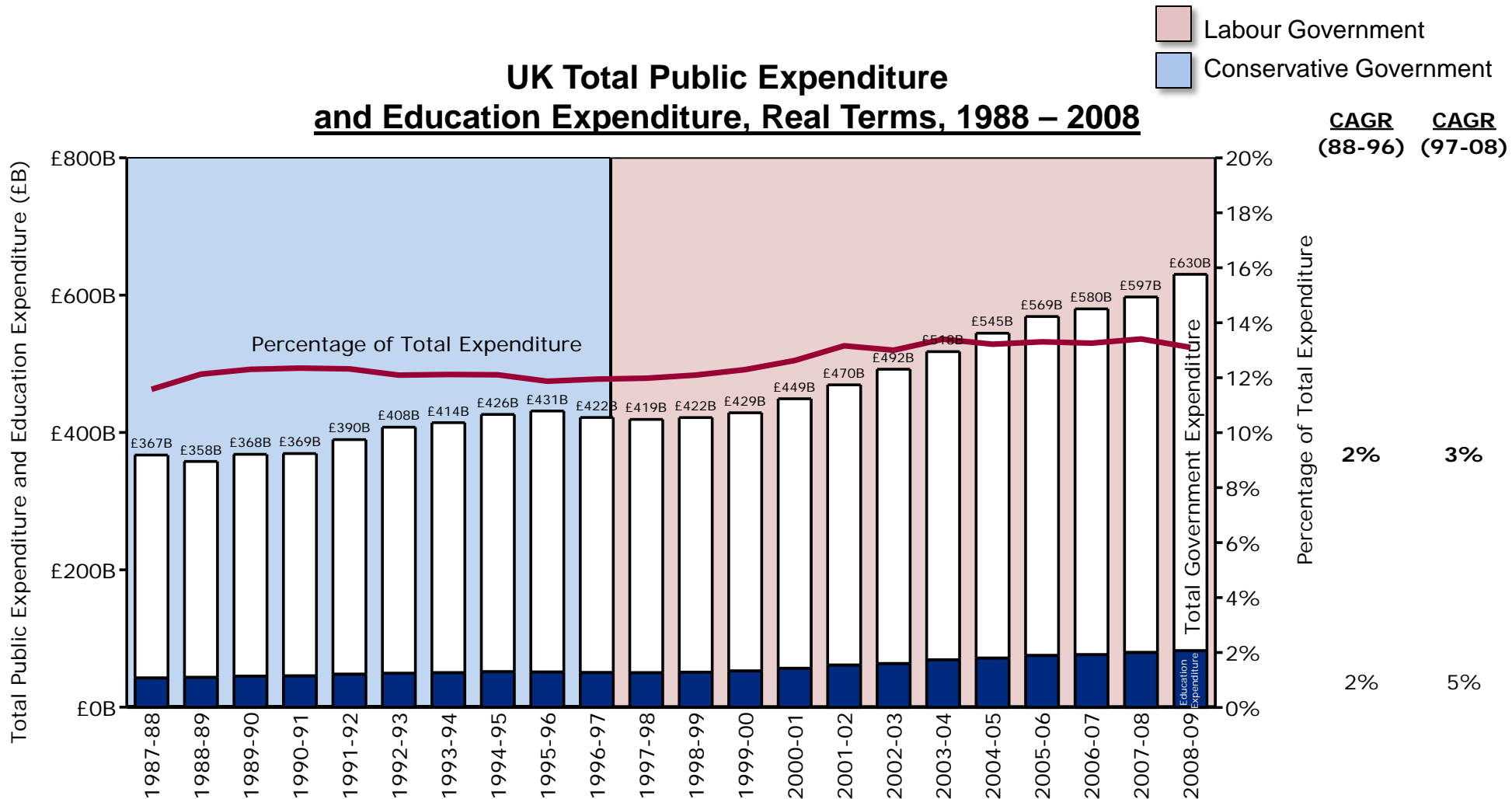
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The Labour government increased education spending at a slightly higher annual rate than the previous Conservative government



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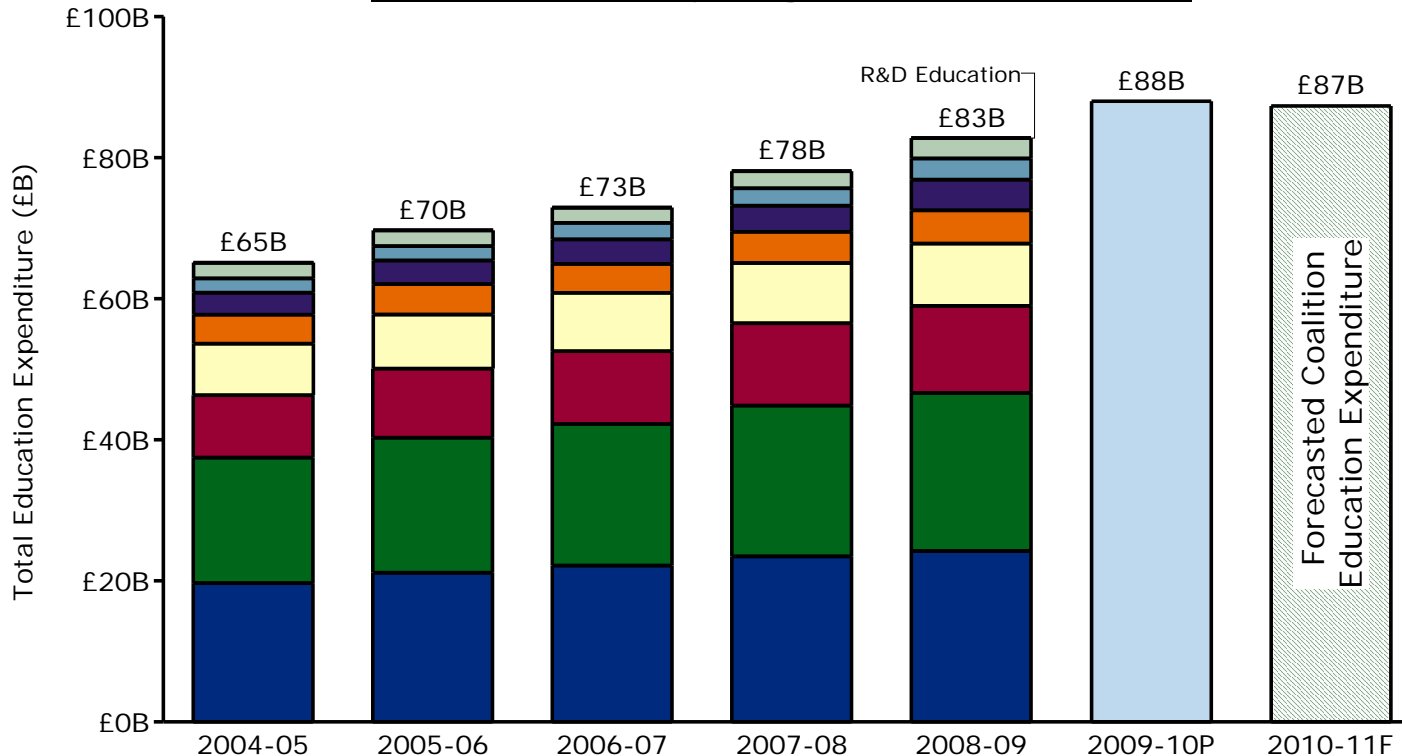


Under Labour, funding witnessed strong growth across the board. Tertiary education was a key beneficiary



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UK Government Education Expenditures, by Segment, 2004 – 2011F



CAGR
(04-08)

6%
-18%

CAGR
(09-10)

-1%

- 7% 10% 9% 3% 5% 9% 5% 6%
- General
- Other.
- Subsidiary Services
- Pre-Primary
- Post-Secondary, Non-Tertiary
- Tertiary
- Primary
- Secondary

3-19 Year Olds	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10P	2010-11F
	12.8MM	12.7MM	12.7MM	12.6MM	12.5MM	12.4MM	12.4MM

Coming into the current fiscal year, the previous Labour government committed modest growth in education funding



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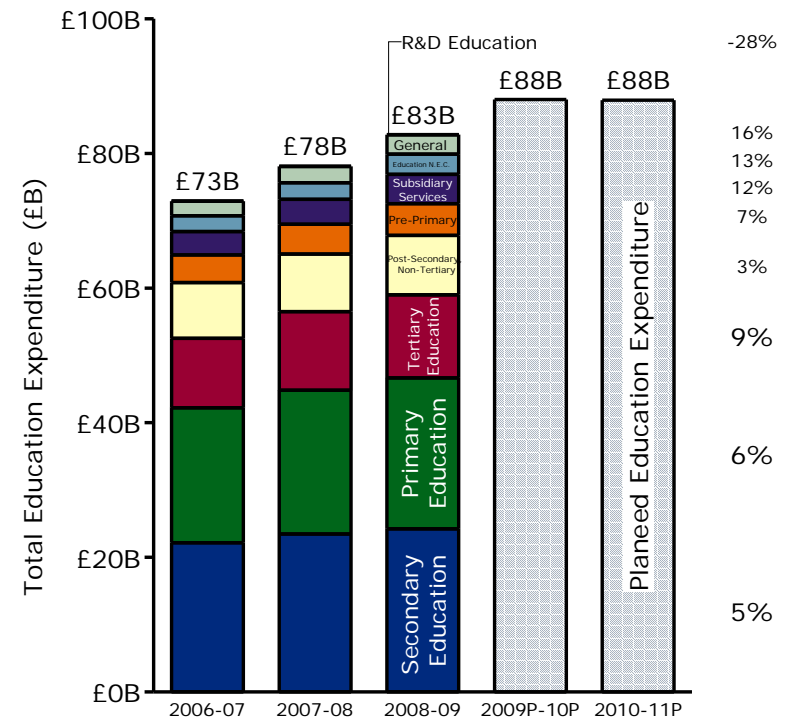
Tradition

- “Education, education, education”
- **Building Schools for the Future:** Pledge to rebuild/renew all 3,500 secondary schools in England by 2020
- **School Standards:** National Literacy and Numeracy Strategies successfully increased standards, especially for boys
- **Parental Choice:** ‘Freedom for schools and power for parents’ as key Labour themes
- **Staying On:** Emphasis on reforming education for 14-19 year olds, based on view that too many students leave school early and with a low grasp of basic skills
- **Universities:** £270MM University Modernisation Fund – designed to fund an extra 20,000 university places

Manifesto

- Increase funding for frontline Sure Start, schools, and 16-19 learning
- One-to-one and small-group tuition guaranteed
- Raise education and training leaving age to 18
- £270MM for universities, 20,000 new university places
- Extend Teach First, a scheme to recruits top graduates
- Parental ability to bring in new school leadership
- Extend Building Schools for the Future programme
- ‘Pupil Premium’ to provide extra funding for disadvantaged pupils

UK Public Education Expenditure, Real Terms, 1997 – 2008 CAGR (06-08) **7%** CAGR (06-10) **5%**



Leading up to the General Election, both coalition parties made commitments to education reform that will have major impact



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Primary & Secondary

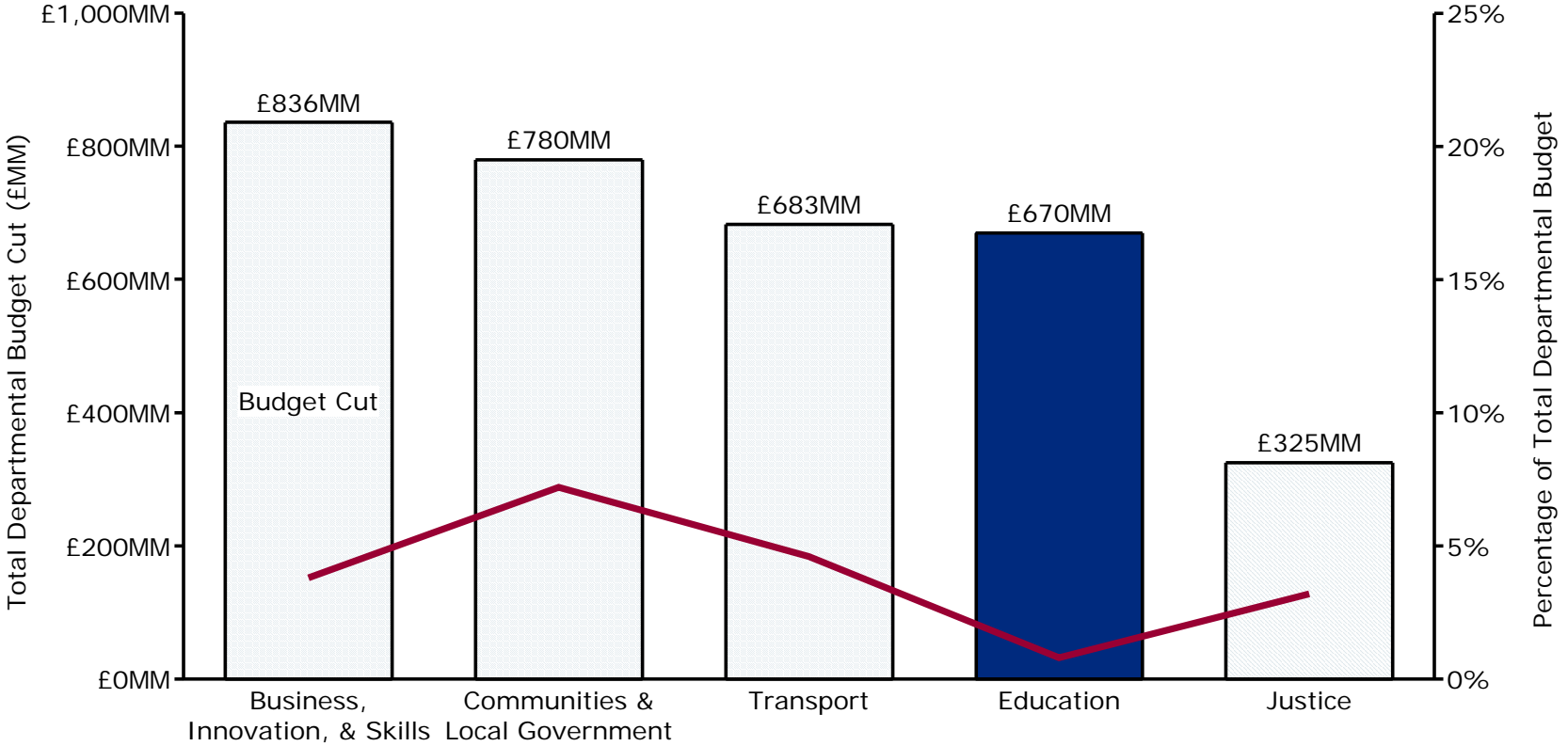
Tertiary

- **Focus:** Equal opportunity regardless of background; more freedom to schools
- **Grassroots commitment to local oversight**
- £2.5B for 'Pupil Premium'
- Axe the National Curriculum, reform league tables
- Allow establishment of new faith schools, with inclusive admissions policies
- **Focus:** Classroom discipline, new generation of independently run state schools
- **Shift responsibility away from Local Authorities**
- 'Pupil Premium'
- Reform National Curriculum, reform league tables
- Expand Academies; establish 'Free schools'
- Recruit better teachers, enforce tougher discipline
- Phase-out university tuition fees
- University tuition fee policy to be announced following Lord Browne's review

In light of the fiscal deficit, the Coalition Government has already announced that education expenditure will be cut modestly - the 2010-11 budget will be cut by ~1%



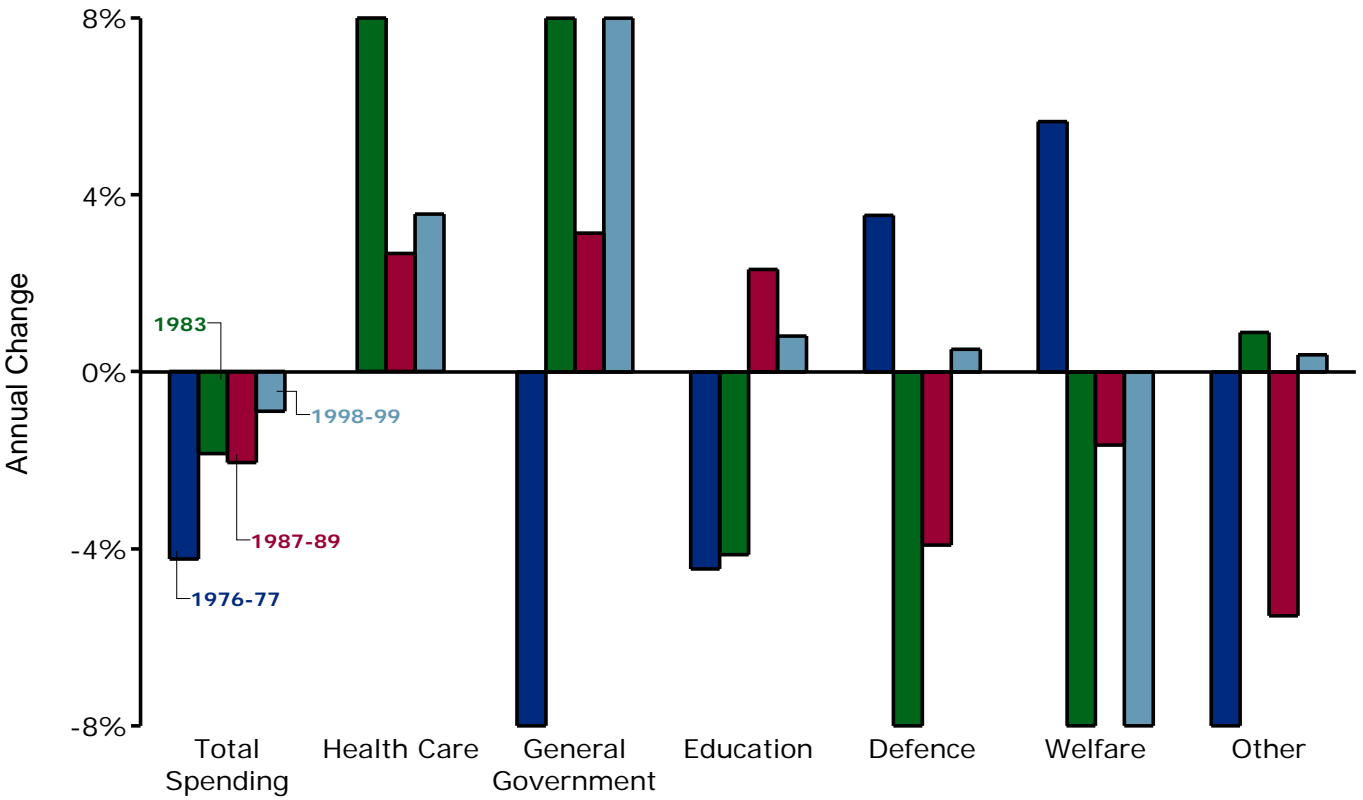
Planned Budget Cuts, By Government Department, 2010-2011P



Whilst education spending has been relatively resilient throughout previous government spending cut cycles, given the size of the fiscal deficit, further cuts are expected



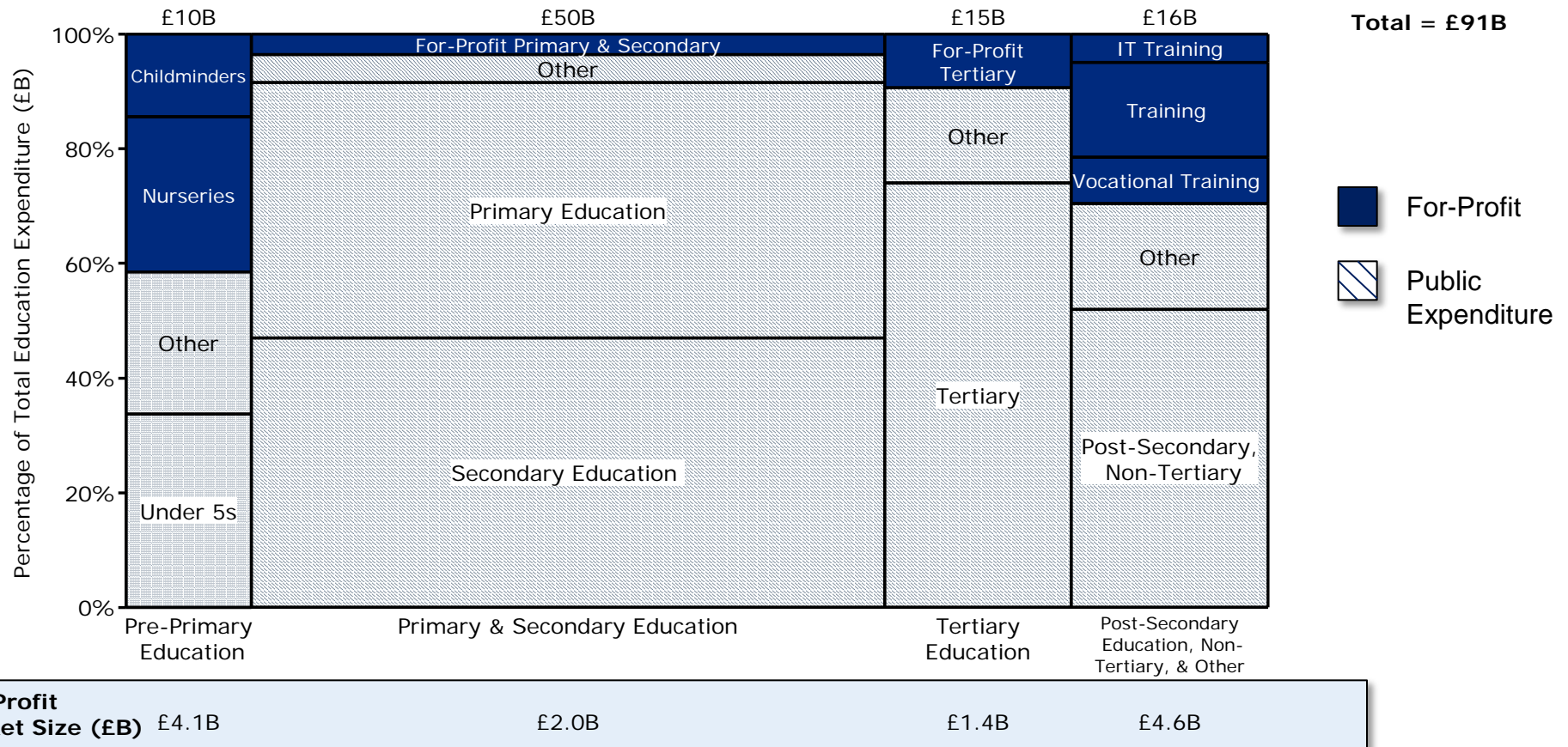
UK Public Expenditure in Previous Cut Cycles, Real Terms



The majority of education spending has historically come from the public sector, with the private sector making up ~10% of total expenditure



UK Public and For-Profit Education Expenditure, by Segment, 2008 – 2009

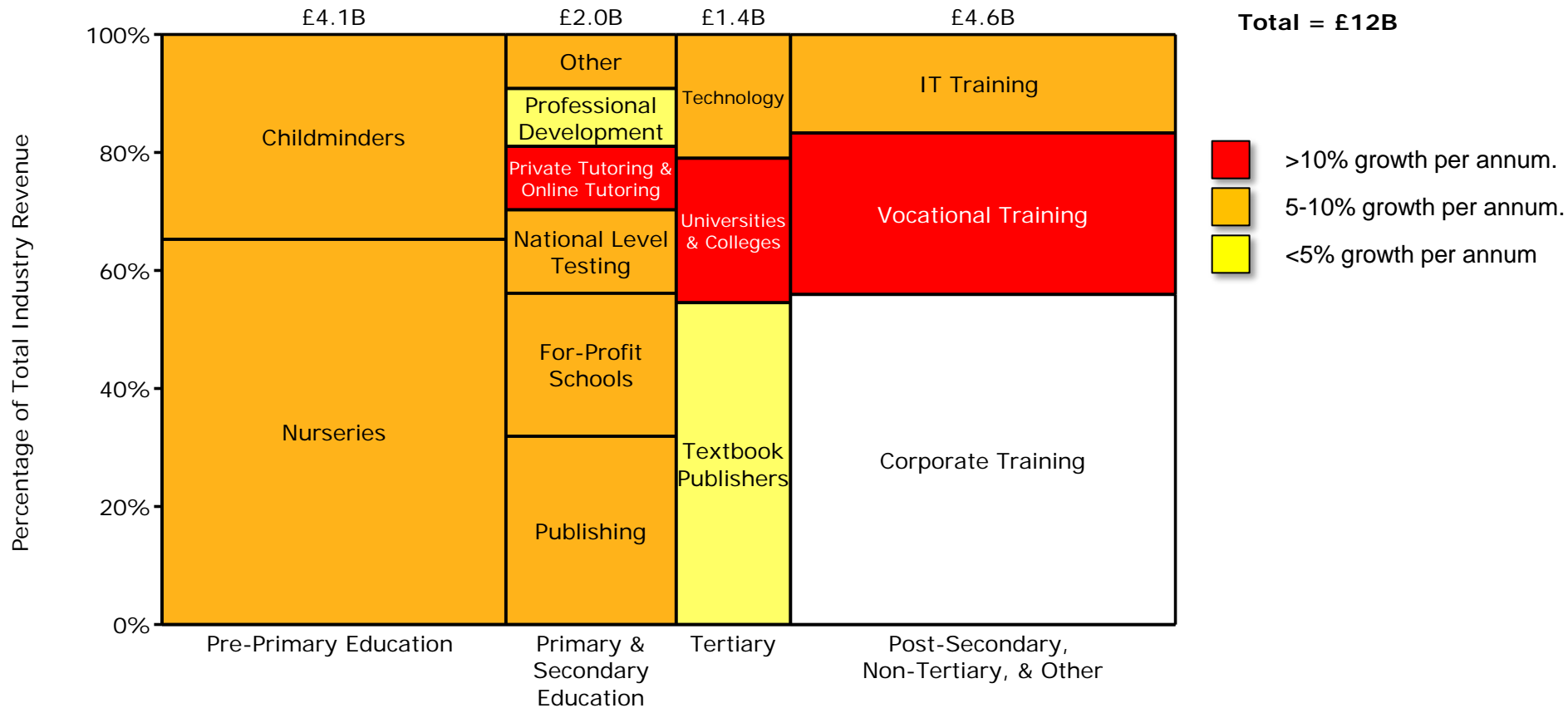


Pre-primary and post-secondary, non-tertiary education dominate the for-profit market, with high growth seen historically in vocational training



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UK For-Profit Education Expenditure, by Segment, 2007 – 2008



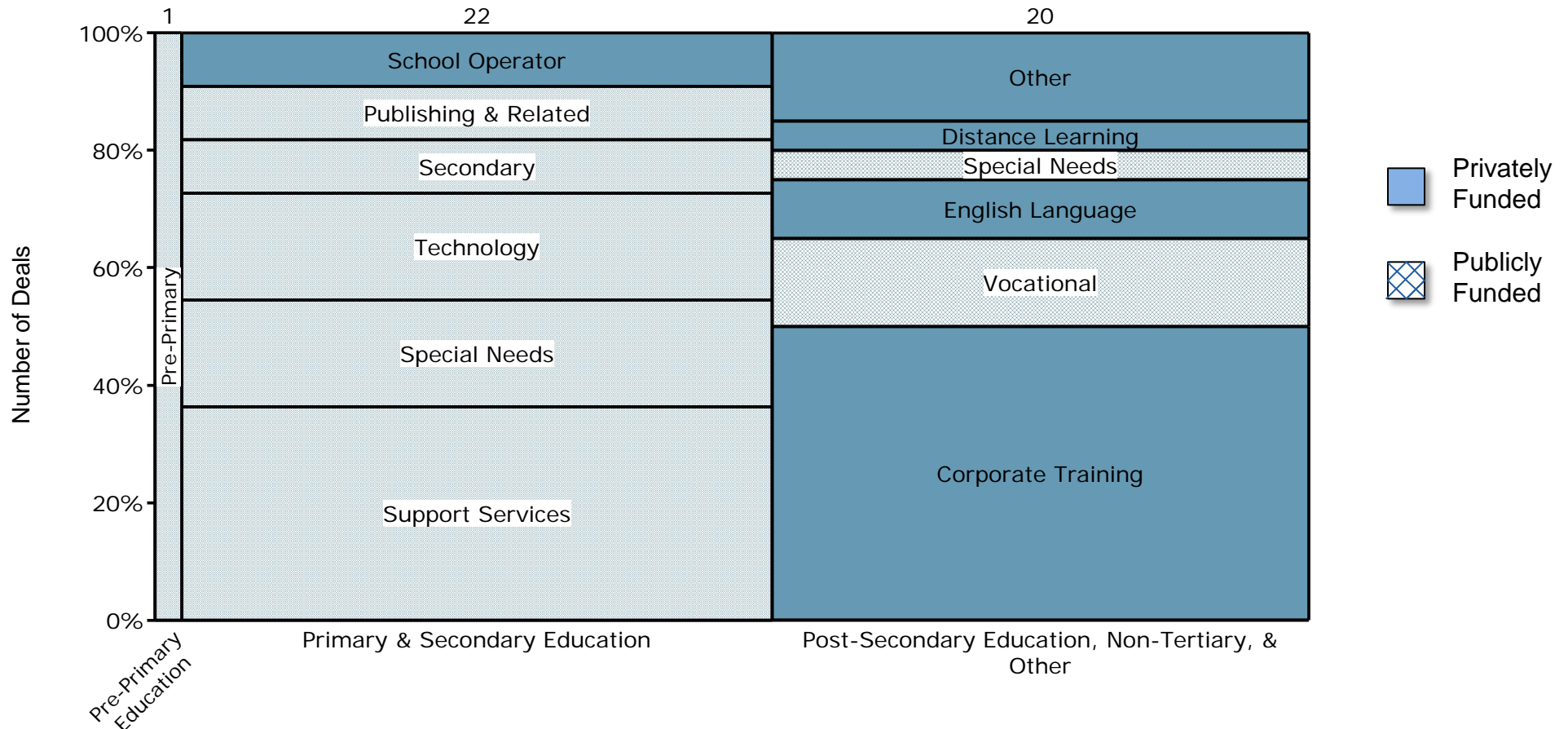
Scale and growth in for-profit segments have been reflected in recent PE activity



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Number of PE Deals in Education by Sector, 2004 – 2010YTD

Total = 43



Note: * Includes some privately funded education

Source: Mergermarket, ThomsonOne

Despite the backdrop of funding cuts, there are still attractive investment opportunities in the UK education sector



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Consolidation in the Vocational Skills Training Market

Emergence of For-Profit Private Higher Education Institutions

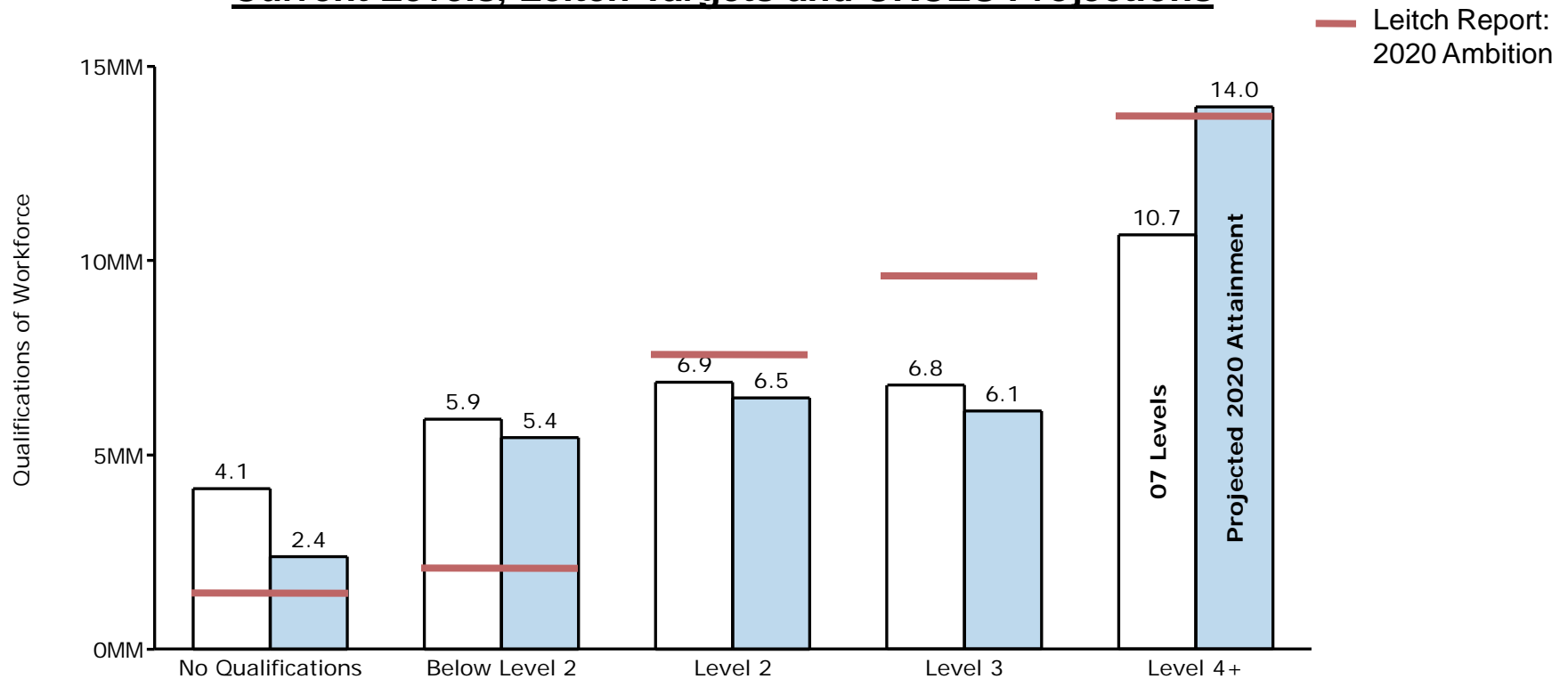
Expected Role of Private Operators in the Academies Programme

Leitch targets show that a considerable 'skills gap' remains in the UK, underscoring a market for vocational skills training



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**UK Qualifications Projections 2007 - 2020:
Current Levels, Leitch Targets and UKCES Projections**

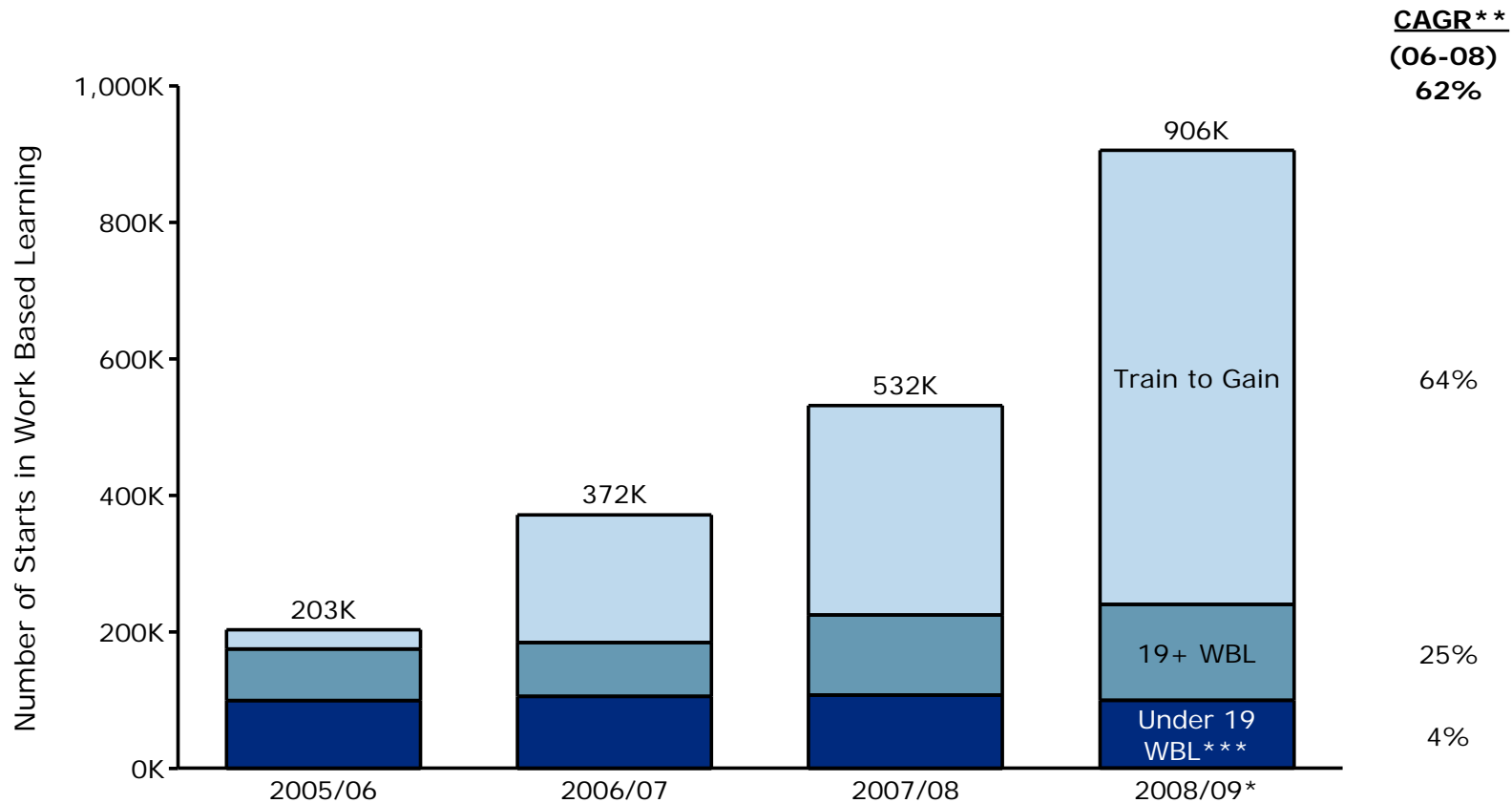


In light of the 'skills gap', we have seen a rapid rise in the number of learners entering vocational skills training, with Train to Gain a key driver



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Number of Starts in Work Based Learning, 2005/06 – 2008/09



Note: Learner numbers refer to the total number of new starters during the year; Learners starting more than one framework will appear more than once; Train to Gain numbers *exclude* participants in Skills for Life; * Train to Gain figures for 2008/09 onwards are not comparable with earlier years as from 2008/09 NVQs delivered in the workplace previously funded by FE are now funded by Train to Gain (there were 181,000 starts in NVQs delivered in the workplace in 2007/08); **Train to Gain growth rate calculated from 2006-07 to 2007-08; *** Includes Under 16 Apprenticeships

Whilst funding has increased significantly in recent years, the outlook is now more uncertain



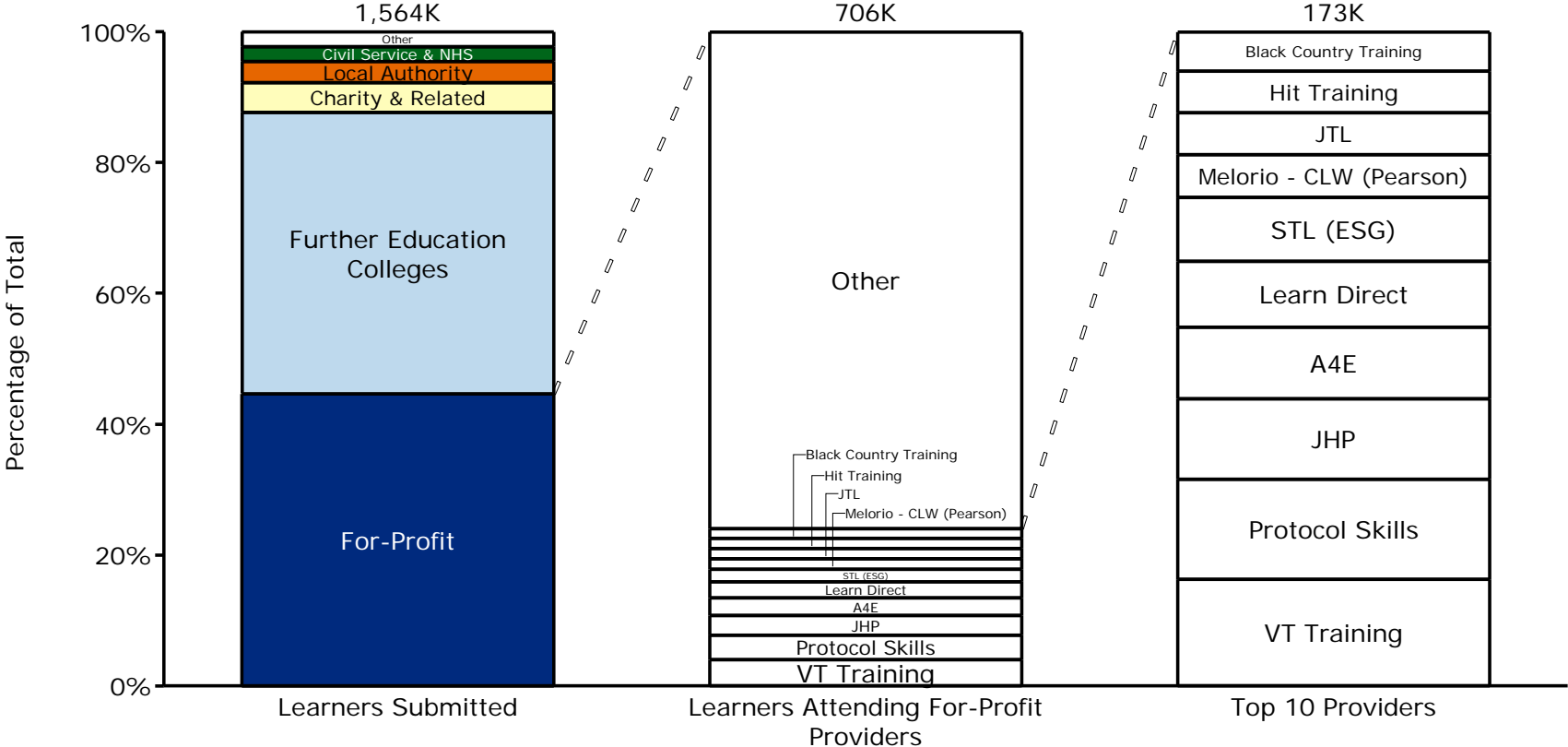
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The vocational skills training sector is highly fragmented. The revised funding outlook is expected to lead to consolidation, with Pearson a recent entrant



Train to Gain and Apprenticeships, Trainees Submitted, by Type and Provider, 2009



Despite the backdrop of funding cuts, there are still attractive investment opportunities in the UK education sector



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Consolidation in the Vocational Skills Training Market

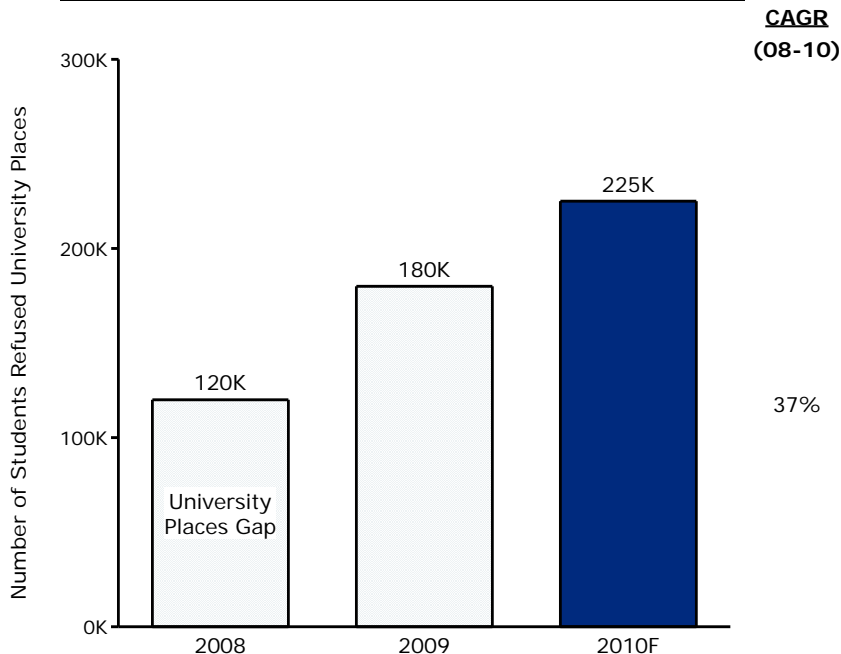
Emergence of For-Profit Private Higher Education Institutions

Expected Role of Private Operators in the Academies Programme

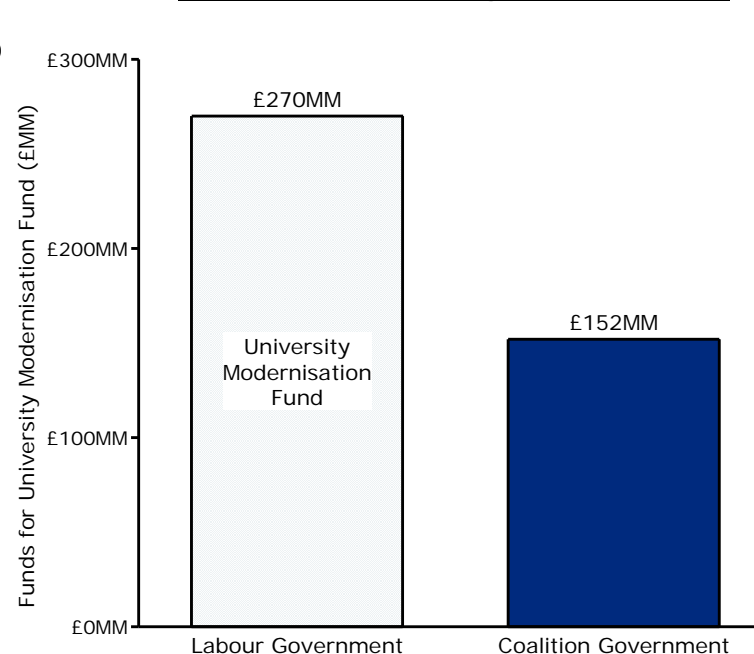
Unmet demand for university places continues to increase. However funding looks set to fall...



University Places Gap - Number of Applicants Without Seats, 2008 – 2010



University Modernisation Fund, Planned Spending, 2009 – 2010



- Coalition Government announced plans to cut £200MM from this year's higher education budget
- The £270MM University Modernisation Fund - designed to fund an extra 20,000 places - was singled out for cuts
- The Fund will be cut by £118MM and extra places reduced to 10,000 (from 20,000), with a further £82MM in cuts planned
- With applications increasing (+16.5% from last year), the number of applicants refused a university place is expected to increase from 180K in 2009 to ~250K in 2010

Prospects for private higher education providers in the UK are expected to improve, as demand outstrips supply for British qualifications



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Overview

Current Situation

Outlook

Higher Education Colleges

- 130 Higher Education colleges whose offerings include degree courses (BA, MA, PhD, etc.), Diplomas, Certification, and degree pathway programmes
- All degrees accredited / validated by public universities

- Accredited by the British Accreditation Council (BAC) and partner with universities to confer degrees
- Number of private colleges increasing rapidly, with many looking to become degree granting institutions

- UK private higher education sector is evolving rapidly, driven, in part, by foreign students seeking British degrees. For example, Holborn College in London registers ~1,500 full-time-equivalent students, 98% of which are international students

Degree Awarding Institutions

- 5 universities, University of Buckingham, BPP, College of Law, Ashridge Business School, and IFS School of Finance have degree awarding powers
- Currently BPP (acquired by Apollo Global last year) is the only for-profit institution, whilst the others operate as not-for-profit institutions

- Student numbers and profitability have been growing, with education companies in the UK weathering the recession better than many other sectors
- Apollo's acquisition of BPP "has sent a signal to its large American counterparts that the UK market is worth watching"

- Given the likely rise of the undergraduate university tuition fees cap as well as the widening gap in places available at universities for applicants, private universities are likely to become more attractive to students and investors
- Pressure will likely mount on the government to loosen restrictions relating to degree granting status

Despite the backdrop of funding cuts, there are still attractive investment opportunities in the UK education sector



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Consolidation in the Vocational Skills Training Market

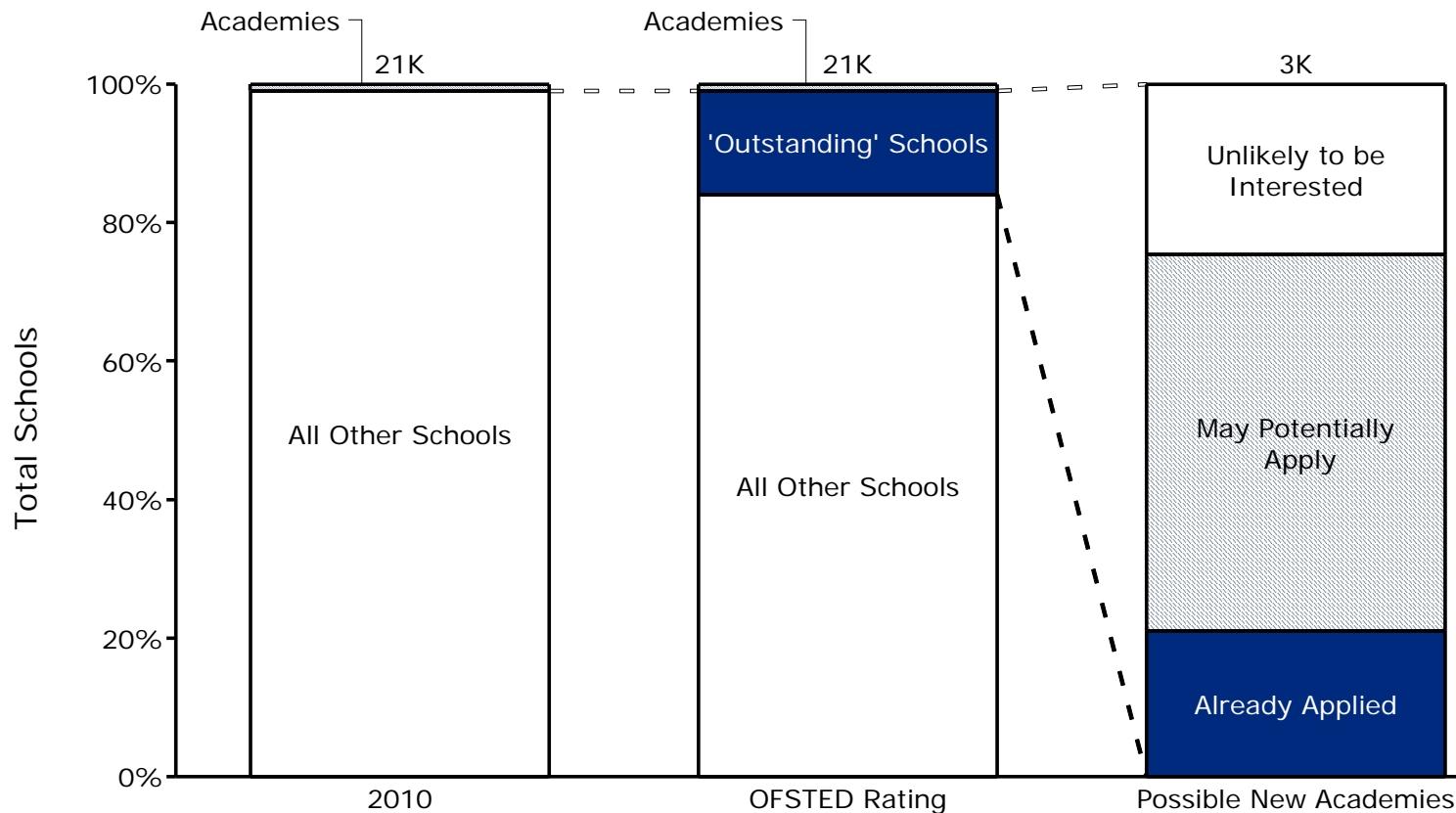
Emergence of For-Profit Private Higher Education Institutions

Expected Role of Private Operators in the Academies Programme

The number of academies seems primed to drastically increase – surveys of head teachers put the figure at 2000+



Number of Schools, OFSTED Ranking and Academies Potential, 2010



- 626 'Outstanding' schools applied for Academy status in the week following Michael Gove's proposal
- Based on a TES survey of school head masters, another ~1,400 'Outstanding' schools will consider applying for Academy status
- Total number of 'Outstanding' schools who may become Academies in the near future is ~2200

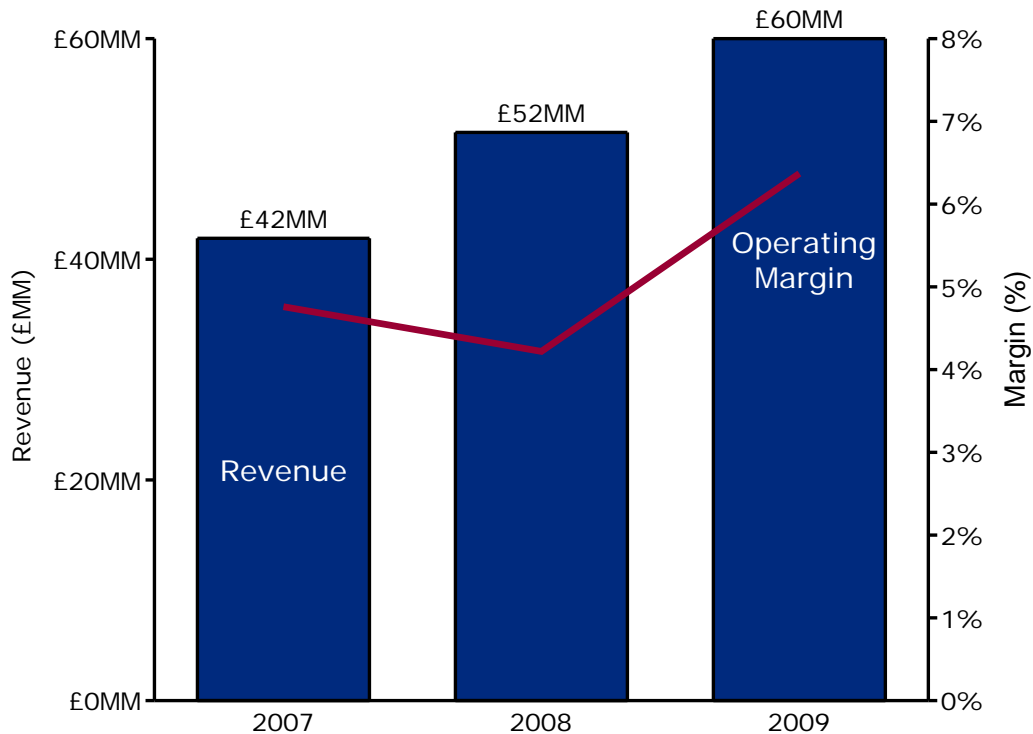


Swedish provider Kunskapsskolan is looking to become a significant operator of Academies in the UK market



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Kunskapsskolan, Revenue and Operating Margin, 2007 – 2009



Kunskapsskolan Overview

- **Founded in 1999, Kunskapsskolan operates ~30 schools in Sweden**
 - Schools are state-funded, free of charge, non-selective, and financed through a state school voucher system, entitling parents to choose schools
- **Opened offices in London in 2007. Three current schools are in the process of becoming Academies:**
 - Hampton Community College and Whitton School to open as Academies from September 2010
 - Holywells High School: Selected by Suffolk County Council as the preferred sponsor for the proposed Academy at Holywells
- ***“[Kunskapsskolan] has its eye on five new schools in Cambridge and more in the Thames Gateway house-building scheme. The ambition is for 30 academies as well as a handful of profit-generating independent schools in England over the next 10 years”***
 - Guardian, April 2008